STATE OF ILLINOIS
OFFICE OF THE
AUDITOR GENERAL
William G. Holland, Auditor General

SUMMARY REPORT DIGEST

DEPARTMENT OF CENTRAL MANAGEMENT SERVICES

Financial Audit
For the Year Ended: June 30, 2011
Compliance Examination
For the Two Years Ended: June 30, 2011

Summary of Findings:

Total this audit:	**16**
Total last audit:	**19**
Repeated from last audit:	**12**

Release Date: April 26, 2012

INTRODUCTION

This report covers our financial audit for the year ended June 30, 2011 and compliance examination for the two years ended June 30, 2011 of the Department of Central Management Services.

SYNOPSIS

- The Department's year-end financial reporting to the Office of the State Comptroller contained significant errors.
- The Department lacked adequate justification for the cancellation of a Request for Proposal for temporary staffing services.
- The Department overpaid employees that were on a leave of absence.
- The Department failed to file reports as required by statute.
- The Department did not comply with the Fiscal Control and Internal Auditing Act.

{Expenditures and Activity Measures are summarized on the reverse page.}

DEPARTMENT OF CENTRAL MANAGEMENT SERVICES
FINANCIAL AUDIT AND COMPLIANCE EXAMINATION
For the Year(s) Ended June 30, 2011

STATEMENT OF ACTIVITIES INFORMATION GOVERNMENTAL ACTIVITIES (expressed in thousands)	Fiscal Year 2011	Fiscal Year 2010	Fiscal Year 2009
PROGRAM REVENUES			
Charges for Services	$ 663,929	$ 746,099	$ 764,124
EXPENSES			
Total Expenses	743,192	986,074	861,767
NET (EXPENSES) REVENUES	**(79,263)**	**(239,975)**	**(97,643)**
Total General Revenues and Transfers	110,575	93,302	76,511
CHANGE IN NET ASSETS	**31,312**	**(146,673)**	**(21,132)**
Beginning Net Assets, July 1, after change in presentation	341,391	(16,002)	5,130
ENDING NET ASSETS, JUNE 30	**$ 372,703**	**$ (162,675)**	**$ (16,002)**

STATEMENT OF NET ASSETS INFORMATION GOVERNMENTAL ACTIVITIES (expressed in thousands)	Fiscal Year 2011	Fiscal Year 2010	Fiscal Year 2009
Cash Equity with State Treasurer	$ 52,811	$ 42,181	$ 38,137
Cash and Cash Equivalents	3,849	3,766	3,670
Capital Assets, net	251,493	265,405	284,217
Other Assets	824,517	253,904	234,279
Total Assets	**1,132,670**	**565,256**	**560,303**
Accounts Payable	89,700	114,559	95,393
Long Term Obligations	639,157	590,896	459,134
Other Liabilities	31,110	22,476	21,778
Total Liabilities	**759,967**	**727,931**	**576,305**
Net Assets, Invested in Capital Assets, Net of Related Debt	218,856	227,783	239,166
Net Assets, Restricted for Debt Service and General Government	3,855	3,766	3,670
Net Assets, Unrestricted	149,992	(394,224)	(258,838)
Total Net Assets	**$ 372,703**	**$ (162,675)**	**$ (16,002)**

SELECTED ACTIVITY MEASURES (Unaudited)	Fiscal Year 2011	Fiscal Year 2010	Fiscal Year 2009
Average Number of Employees (Audited)	1,448	1,575	1,645
Number of Business Enterprise Program Applications Received	1,814	1,989	2,082
Number of Network Data Circuits Managed	7,505	7,866	7,742
Number of Flexible Spending Account Participants	13,509	13,402	13,017
Number of Equipment Items Transferred Out of Surplus	4,129	4,410	3,316
Total Gallons of Gasohol Sold	683,249	744,826	770,800
Number of Facilities Participating in I-cycle	283	254	254

AGENCY DIRECTOR

During Examination Period: Mr. James Sledge (7/1/09 - 6/16/11), Mr. Malcolm Weems (Acting) (6/16/11 - current)
Currently: Mr. Malcolm Weems (Acting)

FINDINGS, CONCLUSIONS, AND RECOMMENDATIONS

WEAKNESSES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

Significant errors in year-end financial reporting

The Department's year-end financial reporting in accordance with generally accepted accounting principles (GAAP) to the Office of the State Comptroller contained significant errors in the determination of certain year-end account balances and note disclosures.

During our audit of the June 30, 2011 financial statements, we noted material weaknesses and significant deficiencies resulting from the Department's failure to establish adequate internal control over the accumulation of information necessary for the proper reporting of financial information as follows:

Methodology for calculating the pension-type awards liability not reasonable

Fiscal year 2011 workers' compensation liability understated $69 million

- The Department is responsible for recording a liability for workers' compensation claims for injuries incurred before year-end that are probable of resulting in an award. This liability is to include estimated losses for pending or claims considered to be in the process of being awarded at the end of the fiscal year as well as estimated losses for claims that are unreported at year-end. The Department currently uses a methodology that includes an estimate of pension-type awards likely to be paid for injuries already incurred. The Department estimated this portion of the total workers' compensation liability by calculating an average annual number of new awards being paid over the last five fiscal years. Utilizing this methodology, the Department has estimated only 36 pension-type awards with a cost of $24 million that will be made in the future for injuries incurred prior to June 30, 2011. This methodology does not include any consideration of historical information relating to the date of the injury to the period when pension-type payments would begin. Based on information maintained by the Department relating to current pension-type awards being paid, it takes in excess of three years from the date of injury before payments begin on pension-type awards for 87% of the claims. As such, we believe claims with approximate awards of $93 million represent a more reasonable estimate of the future pension-type awards to be made for injuries incurred prior to June 30, 2011. This results in an understatement of the liability in the Department's financial statements of approximately $69 million. The estimate would be more accurate if actuarially calculated based on projected outcomes based on facts and circumstances inherent in the individual claims and by applying a consistent and supported assessment of those individual claims. The Department has adjusted the financial statements to record the additional liability.

Several other financial statement errors noted

- We noted several other errors in the preparation of the Department's financial statements. The errors included improperly calculating the amount reported as "invested in capital assets, net of related debt," overstating accounts payable, failure to eliminate all inter-department charges for internal service fund activity, errors in the allocation of functional expenses, and errors in the calculation of the current year lease payments and the future minimum lease payments in the operating leases footnote. The errors noted were not individually significant to the financial statements taken as a whole; however, the Department did not have effective controls over the reconciliation and review functions to ensure amounts were properly reported at June 30, 2011.

Inventory physical counts not performed

- The Department did not perform a physical count of the commodities inventory on hand at any of the twelve commodity storage locations and was unable to provide a value of the inventory on hand at June 30, 2011. The Department also has not developed or maintained oversight policies and procedures regarding the commodities inventory. (Finding 1, pages 14-16 of the Compliance Report) **This finding was first reported in 2007.**

We recommended the Department implement procedures to ensure GAAP Reporting Packages prepared and submitted to the Office of the State Comptroller for financial reporting purposes are complete and accurate. We further recommended the Department utilize an actuary to estimate the workers' compensation liability or establish a methodology to more reasonably estimate the outstanding pension-type workers' compensation liability by utilizing a case-by-case analysis for known claims and more relevant historical information for other probable claim losses.

Department agrees with auditors

Department officials concurred with our recommendation and stated that they have addressed each of the control recommendations. In addition, the Department plans to contract with an actuary for assistance with future Workers' Compensation liability calculations. (For the previous Department response, see Digest Footnote #1)

INADEQUATE JUSTIFICATION FOR THE CANCELLATION OF A MASTER CONTRACT PROCUREMENT

Lacked justification for the cancellation of a RFP

Department limited competition

The Department lacked adequate justification for the cancellation of a Request for Proposal (RFP) for temporary staffing services. In addition, the Department effectively limited competition in the subsequent Invitation for Bid (IFB) through establishment of criteria which ultimately resulted in the disqualification of all but one vendor.

Original RFP cancelled without justification

Contract under IFB subsequently awarded

During the current period, the procurement and award files for 14 solicitations, contracts, or renewals awarded in fiscal years 2010 and 2011 were selected for testing, totaling a maximum award amount of approximately $339.3 million. In 1 of the 14 (7%) contracts reviewed, a $12.7 million, (including potential extensions) master contract to provide temporary staffing services for Cook County, the Department cancelled the original RFP procurement without adequate justification and subsequently awarded a contract under an IFB that effectively limited competition. The RFP/IFB specifications included estimated hours for various base services plus estimated additional skills to be provided under the contract. (Finding 4, pages 21-24 of the Compliance Report)

We recommended the Department establish appropriate controls to ensure the procurement process is conducted in a fair and open manner that does not restrict or exclude any potential bidders.

Department agrees with auditors

Department officials concurred with our recommendation and stated that the Department agrees that appropriate controls are necessary to ensure that procurement processes are conducted in a fair and open manner that does not restrict competition. This is a commitment taken very seriously within the agency and processes are in place to sufficiently and effectively monitor RFP and IFB execution. The Department also stated that the decision to cancel the RFP was related to statewide efforts related to cost containment and the Department determined cancellation to be in the best interest of the State. This was done and approved with review and input of numerous members of agency leadership. The Department agreed that this approval should have been better documented.

WEAKNESSES IN CONTROLS OVER PAYMENTS TO EMPLOYEES RELATED TO LEAVE OF ABSENCES

The Department did not timely ensure employees on leave of absence were properly reported in the payroll system which resulted in overpayments to the employees.

We tested 60 employees that took a leave of absence during fiscal years 2010 and 2011 noting 5 (8%) employees were not

$7,237 overpaid to employees on leave of absence

included in the payroll system properly. The employees were overpaid a total of $7,237 requiring the employee to subsequently reimburse the State for compensation improperly received as follows:

Overpayment reimbursed 2 years later

- One employee returned from an interim assignment-leave of absence on July 25, 2009 but received compensation for the entire pay period resulting in an overpayment for five workdays totaling $1,252. The overpayment was not reimbursed to the State until September 30, 2011.

Overpayment has not been reimbursed to the State

- One employee started a service-connected disability leave of absence on March 29, 2010 but received compensation of $1,374 for the next pay period. The Department did not identify the overpayment until June 15, 2010 and the employee still owes the State.

- One employee started a non-service disability leave of absence on August 26, 2009 but received compensation for the entire pay period resulting in an overpayment for three workdays totaling $820. The Department did not identify the overpayment until May 2010 at which time the employee reimbursed the State.

Overpayments not identified until approximately 9 months later

- One employee started a non-service disability leave of absence on January 14, 2011 but received compensation for the entire pay period resulting in an overpayment for one workday totaling $315. The Department did not identify the overpayment until September 2011 at which time the employee reimbursed the State.

- One employee started a non-service disability leave of absence on January 14, 2011 but received compensation of $3,476 for the next pay period. The Department did not identify the overpayment until October 2011 and the employee still owes the State. (Finding 5, pages 25-26 of the Compliance Report)

We recommended the Department improve controls over leave of absence reporting to ensure employees are properly compensated in accordance with policy and recoup overpayments which remain outstanding.

Department agrees with auditors

Department officials concurred with our recommendation and stated that the Department will review the system in place to ensure that all paperwork affecting transactions is transmitted in a timely manner to the A & R Shared Services Center for processing. The Department will also review the Payroll process to ensure Payroll accurately recoups all monies owed to the State in a timely manner.

FAILURE TO MEET STATUTORY REPORTING REQUIREMENTS

The Department failed to file reports as required by statute.

During our testing we noted reports required to be completed and submitted by the Department have not been filed as follows:

Reorganization report in regard to energy efficiency responsibilities not filed

- The Executive Reorganization Implementation Act (15 ILCS 15/11) requires "Every agency created or assigned new functions pursuant to a reorganization shall report to the General Assembly not later than 6 months after the reorganization takes effect and annually thereafter for 3 years. This report shall include data on the economies effected by the reorganization and an analysis of the effect of the reorganization on State government. The report shall also include the agency's recommendations for further legislation relating to reorganization." On April 1, 2009, the Governor signed Executive Order 2009-7, "Executive Order to Reduce Energy Consumption in State Facilities." This Order abolished the Interagency Energy Conservation Committee and made the Department responsible for implementing a program to increase energy efficiency, track and reduce energy usage and improve the procurement of energy for all State-owned and State-leased facilities for all agencies. To date no reports have been filed regarding this reorganization.

Identity Protection Policy not submitted

- The Identity Protection Act (5 ILCS 179/37(b)) states "Each agency must provide a copy of its identity-protection policy to the Social Security Number Protection Task Force within 30 days after the approval of the policy." The Department approved its identity-protection policy on May 31, 2011 but the policy has not been submitted to the Social Security Number Protection Task Force as required.

- The Civil Administrative Code of Illinois (20 ILCS 405/405-20(b)) states " the Department under the Director shall formulate a master plan for statistical research, utilizing electronic equipment most advantageously, and advising whether electronic data processing equipment should be leased or purchased by the State. The Department under the Director shall prepare and submit interim reports of meaningful developments and proposals for legislation to the Governor on or before January 30 of each year." The Department has not submitted the reports to the Governor as required. (Finding 8, pages 30-31 of the Compliance Report)

We recommended the Department comply with the State statutes and submit all required reports on a timely basis or seek legislative remedy to have the statutory requirement removed.

Department agrees with auditors

Department officials concurred with our recommendation and stated that the Department has developed a strategic initiatives document and submitted it to the Governor's Office. In addition, the Department will make every effort to update this document and submit it within the required time frames. With regard to the Identity Protection Act, the policy was submitted on December 21, 2011. Additionally, CMS's Bureau of Legal Services has created a comprehensive spreadsheet centrally indicating all reporting requirements and deadlines.

NONCOMPLIANCE WITH THE FISCAL CONTROL AND INTERNAL AUDITING ACT

The Department did not comply with the Fiscal Control and Internal Auditing Act (Act) that requires audits of major systems of internal accounting and administrative control.

Audits of major systems not completed

The Department could not demonstrate that audits of major systems were being completed once every two years as required by the Act and certain risk assessment processes lacked sufficient documentation as follows:

- The fiscal year 2011 internal audit plan identified 11 high risk audits to be performed. The Department has not completed or issued any of these 11 audits through the date of this report.

- Subsequent to June 30, 2011, the Department issued reports for audits substantially completed during fiscal year 2011 that were not included in the internal audit plan.

Risk assessments for the eleven major transaction cycles not adequate

- The Department could not demonstrate they were effectively assessing risks associated with the eleven major transaction cycles identified in the Statewide Accounting Management System (SAMS) Manual (Procedure 02.50.20). The risk assessment was general in nature rather than specific to the major transaction cycles.

- The Department could not demonstrate reviews of the design of major new electronic data processing systems or major modifications to existing systems were being performed to ensure the systems provide adequate audit trails and accountability. Discussion of priority projects being administered by the Bureau of

Communications and Computer Services was conducted in bi-weekly meetings, however, no documentation was maintained to support a decision to conduct or not conduct an audit.

Annual report not submitted

In addition, the Act requires annual reports to be submitted to the chief executive officer by September 30 for the prior fiscal year. The annual report for fiscal year 2011 which would have been due September 30, 2011, was not submitted. (Finding 9, pages 32-34 of the Compliance Report) **This finding was first reported in 2006.**

We recommended the Department ensure audits of all major systems of internal accounting and administrative control are conducted at least once every two years and that annual reports are submitted to the chief executive office by September 30 of each fiscal year as required by the Fiscal Control and Internal Auditing Act. We further recommended the Department improve documentation of the risk assessment process to more clearly associate the internal audit effort with identified/assessed risks.

Department agrees with auditors

Department officials concurred with our recommendation and stated that to address the recommendation Internal Audit (IA) plans to take corrective action by implementing new processes by the end of fiscal year 2012. All of the procedures will be updated and documented in the Internal Audit's Policy and Procedure Manual to be followed and carried out going forward. (For the previous Department response, see Digest Footnote #2)

OTHER FINDINGS

The remaining findings are reportedly being given attention by the Department. We will review the Department's progress toward implementation of our recommendations during our next audits.

AUDITORS' OPINION

Our auditors stated the Department's financial statements as of and for the year ended June 30, 2011 are fairly presented in all material respects.

STATE COMPLIANCE EXAMINATION – ACCOUNTANTS' REPORT

The auditors qualified their report on State Compliance for finding 11-1. Except for the noncompliance described in this finding, the auditors state the Department complied, in all material respects, with the requirements described in the report.

WILLIAM G. HOLLAND
Auditor General

WGH:TLD:rt

SPECIAL ASSISTANT AUDITORS

Sikich, LLP were our special assistant auditors.

DIGEST FOOTNOTES

#1 –Weaknesses in Internal Control Over Financial Reporting –Previous Department Response

The Department concurs with the recommendation. We note that, except for the findings related to Workers' Compensation calculations, the exceptions detailed above were not material to the Department statements or the Statewide statements. However, we have addressed each of the control recommendations in the following manner: The Bureau of Benefits has corrected the errors in the financial statements pertaining to the Workers' Compensation program. A methodology has been developed to predict future liabilities for pending injuries, in compliance with GASB 10. We are reconciling our pensioner list on a quarterly basis to find any accidental formula omissions. We have increased and will continue to improve training and awareness among fiscal and Shared Services Accounting staff regarding proper treatment of transactions impacting financial statements, particularly during lapse period. In addition, we are implementing more stringent reviews of financial reports before transmission to the Office of the Comptroller so that adjustments are correct and amounts are recognized in the appropriate fiscal year for financial reporting.

#2 –Noncompliance with the Fiscal Control and Internal Auditing Act

Annually, IOIA identifies major FCIAA categories for the 38 agencies it audits. We perform a risk assessment in accordance with the Institute of Internal Audit standards to determine audit coverage for the year, track FCIAA coverage for all audits performed and monitor status continually throughout the year. Changes to the annual audit plan are documented using an "Audit Change Form" or an "Add Audit or Activity to Plan Form". A major consideration specific to the FY09 plan was the American Recovery and Reinvestment Act (ARRA). A considerable amount of time was necessary to research and determine the impact to the State of Illinois. In FY10, ARRA is a component in the annual audit plan. We will continue to assess our operations and implement improvements as needed.